SUPREME COURT, U.S.

No. 150

JUL 14 1961

JAMES R. BROWNING, Clerk

In the Supreme Court of the United States

OCTOBER TERM, 1961

THOMAS E. SNYDER SONS CO., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 41-52[1]) are reported at 34 T.C. 400. The opinion of the Court of Appeals (Pet. App. 1-9) is reported at 288 F. 2d 36.

JURISDICTION

The judgment of the Court of Appeals was entered on March 17, 1961. (Pet. App. 10). The petition for a writ of certiorari was filed on June 15, 1961. The

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[1] "R." refers to the appendix to the petitioner's brief in the court of appeals.

jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a corporation's net operating loss carryovers were properly disallowed pursuant to Section 129 of the 1939 Code and Section 269 of the 1954 Code, on the ground that the owner of the corporation had acquired control of it for the principal purpose of avoiding federal income taxes.

STATUTES INVOLVED

Section 129 of the Internal Revenue Code of 1939 and Sections 269 (a) and (b) of the Internal Revenue Code of 1954 are set out in the Appendix, *infra*, pp. 9-11.

STATEMENT

The petitioner was organized on March 3, 1949, as "Great American Farm Implement Corp." (R. 42.) Benjamin A. Snyder and his brother each acquired, for $62,500, 625 shares of the total of 1,795 shares issued. (R. 43; Pet. App. 1.) The corporation was organized to develop and market corn pickers and other agricultural machinery. It suffered large net operating losses in each of its fiscal years ended February 28, 1950, 1951, 1952, and 1953, and by the last date was out of business. As of August 1, 1953, the corporation had outstanding debts represented by notes payable aggregating $82,224.37. (R. 43.) Its balance sheet on August 31, 1953, showed an earned surplus deficit of $242,411.30. (R. 45.)

Thomas E. Snyder Sons Company ("Old Snyder") was incorporated in 1941 to engage in the business of transporting and merchandising molasses. (R. 43.)

Benjamin Snyder was the president and sole stockholder of Old Snyder (R. 43.) It operated profitably in its fiscal years ended August 31, 1950, 1951, 1952, and 1953, and the period September 1, 1953, to February 28, 1954 (R. 46).

Between 1949 and 1953, Benjamin Snyder purchased in his own name 45 railroad tank cars. He operated these as a sole proprietor; they were used principally to transport molasses dealt in by Old Snyder. He was paid for the use of these cars on a mileage basis by the railroads over which they traveled. After a small net operating loss in 1949, Benjamin Snyder showed a net operating profit in this business in each of the years 1950, 1951, 1952, and the period of January 1 through March 31, 1953. (R. 44.)

On August 26, 1953, and September 1, 1953, Benjamin Snyder acquired the petitioner's remaining 1170 outstanding shares for a total of $234. (R. 5-6.) On August 25, 1953, he and his brother acquired the petitioner's outstanding notes payable for $3,091. (R. 43.) On September 1, 1953, immediately after acquiring such stock and notes, Benjamin Snyder transferred his 45 tank cars to the petitioner in exchange for a note of $247,258.57. In November, 1953, the petitioner acquired ten more tank cars at a cost of $72,617.60. On September 2, 1953, the petitioner's articles of incorporation were amended to authorize it to engage in the tank car and molasses business. (R. 45.)

From September 1, 1953, to the close of its fiscal year ended February 28, 1954, the petitioner's sole income was from the railroads' payments for tank car mileage. The corporation made a profit, but carried over net operating losses from previous years and reported no income subject to tax. (R. 45-46.)

Effective March 1, 1954, Old Snyder merged into the petitioner, and the latter changed its name to that of Old Snyder, *i.e.*, Thomas E. Snyder Sons Company. (R. 46.) In its fiscal years ended February 28, 1955, and 1956, the petitioner derived a profit from the rental of tank cars and buying and selling molasses. (R. 47.) It also sought to carry over and deduct in those years net operating losses from prior years.

The Commissioner disallowed the net operating loss carry-overs for each of the fiscal years ended 1954, 1955, and 1956. (R. 47.)

The Tax Court unanimously sustained the Commissioner (R. 50-52). It found (R. 47-48) that the business of the petitioner which incurred the losses was "entirely different from its business which produced the income against which it now seeks to offset these losses by means of the net operating loss deduction"; that Benjamin Snyder acquired control of the petitioner in 1953; and that his principal purpose in doing so "was to evade or avoid Federal income tax by securing to himself, as sole shareholder, the benefit of petitioner's net operating loss deductions, a benefit or deduction which he would not otherwise have enjoyed." The court concluded (R. 51) that Section 129 of the Internal Revenue Code of 1939 and Section 269 of the 1954 Code (*infra*, pp. 9-11), which bar the allowance of an operating loss carry-over where control of a corporation is acquired with the principal purpose of evading or avoiding Federal income tax, "require the disallowance of the operating loss carryover."

The court of appeals unanimously affirmed. (Pet. App. 1-9). It held (Pet. App. 4-6) that there was substantial evidence to sustain the Tax Court's findings

that Benjamin Snyder acquired control of the petitioner in 1953, and that "tax avoidance" was "the principal purpose" for such acquisition; and that these findings support the disallowance of the loss carry-over.

ARGUMENT

This case involves primarily the correctness of the Tax Court's factual findings on the year in which Benjamin Snyder acquired control of the petitioner, and his purpose in making the acquisition. The decision of the court of appeals on these issues is correct and in accord with the decisions of other circuits; and the case presents no issue warranting further review.

1. Section 129(a) of the 1939 Code and Section 269(a) of the 1954 Code both provide that if any person acquires control of a corporation for the principal purpose of evading or avoiding income or excess profits taxes by securing a deduction which such person would not otherwise enjoy, such deduction shall be disallowed. The Tax Court held that Benjamin Snyder acquired control of the petitioner in 1953 for that purpose and, as the opinion of the court of appeals makes clear (Pet. App. 4-8), these findings are fully supported by the evidence. In these circumstances, the petitioner's net operating loss carry-overs were correctly disallowed. *Coastal Oil Storage Co.* v. *Commissioner*, 242 F. 2d 396 (C.A. 4); *Commissioner* v. *British Motor Car Distributors, Ltd.*, 278 F. 2d 392 (C.A. 9); *James Realty Co.* v. *United States*, 280 F. 2d 394 (C.A. 8); *Mill Ridge Coal Co.* v. *Patterson*, 264 F. 2d 713 (C.A. 5), certiorari denied, 361 U.S. 816.

The petitioner challenges the disallowance of the deductions on the ground that since Benjamin Snyder

and his brother together acquired more than 50 per cent of the petitioner's stock when the company was organized in 1949, he did not acquire control in 1953, when he was found to have had a tax-avoidance purpose. The Code provisions specifically state, however, that "control means the ownership of stock possessing *at least* 50 per centum of the total combined voting power * * * or *at least* 50 per centum of the total value of shares of all classes of stock * * *" (Section 129(a), 1939 Code, and Section 269(a), 1954 Code, App. *infra*, pp. 9, 11, emphasis added). It was not until 1953, when Benjamin Snyder for the first time individually obtained more than 50 percent of the stock, that he acquired control of the petitioner within the meaning of the foregoing provisions. The petitioner's reliance upon Section 24(b)(2)(B) and (D) of the 1939 Code is misplaced. Those subsections provide that "[a]n individual shall be considered as owning the stock owned, directly or indirectly, by or for his family," and define "family" to include "brothers." But, as the court of appeals pointed out (Pet. App. 4-5), those provisions apply only to deductions for losses from sales or exchanges of property, and not to the net operating losses sought to be deducted in the instant case.

The petitioner further apparently contends that Sections 129(a) and 269(a) apply only where the person acquiring control of the corporation is the taxpayer seeking the benefit of the loss carry-over, and not where, as here, the taxpayer was the corporation whose control was acquired. The statute contains no such limitation, however, but broadly provides for disallowance whenever any "person or persons" acquire control of a corporation for the principal purpose of evad-

ing or avoiding taxes. Four other circuits have passed upon the question, and they are all in accord with the decision below. See the cases cited *supra*, p. 5.

2. The petitioner urges (Pet. 4) that this Court should here decide the question it left open in *Libson Shops, Inc.* v. *Koehler*, 353 U.S. 382, 390, note 9. There the Court, in holding that a corporation which had been merged with other constituent companies could not carry over operating losses of the latter which had been incurred in businesses other than that of the surviving company, left open the situation where "a *single* corporate taxpayer changed the character of its business and the taxable income of one of its enterprises was reduced by the deductions or credits of another." But whether or not this case, involving a merger, presents the question reserved in *Libson Shops*, in any event there is no occasion for the Court to consider it. For wholly apart from whether there was the "continuity of business enterprise" (*Libson Shops*, *supra*, p. 386) necessary to support a loss carryover, the holdings below that Benjamin Snyder acquired control of the petitioner in 1953 for the principal purpose of tax avoidance constituted an independent ground for disallowing the deduction.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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APPENDIX

Internal Revenue Code of 1939:

SEC. 129 [as added by Sec. 128(a), Revenue Act of 1943, c. 63, 58 Stat. 21]. ACQUISITIONS MADE TO EVADE OR AVOID INCOME OR EXCESS PROFITS TAX.

(a) *Disallowance of Deduction, Credit, or Allowance.*—If (1) any person or persons acquire, on or after October 8, 1940, directly or indirectly, control of a corporation, or (2) any corporation acquires, on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately prior to such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation, and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income or excess profits tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then such deduction, credit, or other allowance shall not be allowed. For the purposes of clauses (1) and (2), control means the ownership of stock possessing at least 50 per centum of the total combined voting power of all classes of stock entitled to vote or at least 50 per centum of the total value of shares of all classes of stock of the corporation.

(b) *Power of Commissioner to Allow Deductions, Etc., in Part.*—In any case to which subsection (a) is applicable the Commissioner is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by such subsection, if he determines that such allowance will not result in the evasion or avoidance of

Federal income and excess profits tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, apportioned, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income and excess profits tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraph (1) and in part under paragraph (2).

(26 U.S.C. 1952 ed., Sec. 129.)

nternal Revenue Code of 1954:

SEC. 269. ACQUISITIONS MADE TO EVADE OR AVOID INCOME TAX.

(a) *In General.*—If—

(1) any person or persons acquire, or acquired on or after October 8, 1940, directly or indirectly, control of a corporation, or

(2) any corporation acquires, or acquired on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately before such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation,

and the principal purpose for which such acquisition was made is evasion or avoidance of Federal

income tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then such deduction, credit, or other allowance shall not be allowed. For purposes of paragraphs (1) and (2), control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote or at least 50 percent of the total value of shares of all classes of stock of the corporation.

(b) *Power of Secretary or His Delegate To Allow Deduction, Etc., in Part.*—In any case to which subsection (a) applies the Secretary or his delegate is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by such subsection, if he determines that such allowance will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, apportioned, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraph (1) and in part under paragraph (2).

* * * * *

(26 U.S.C. 1958 ed., Sec. 269.)

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